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Supreme Court of the United States

October Term, 1932. No. 388.

LETCHER SPICER, by Sam Spicer, Guardian and Committee, - - - - - - - - - Petitioner,

vs.

J. BRYAN SMITH, Special Deputy Banking Commissioner and Liquidating Agent of Hargis Bank and Trust Company.

On Writ of Certiorari to the Court of Appeals of Kentucky.

BRIEF FOR THE PETITIONER.

The Guardian of an incompetent World War veteran collected, and deposited in Bank, the veteran's war risk insurance and disability compensation. The Bank became insolvent, closed its doors, and the State Banking Commissioner liquidated it.

The Guardian has a prior lien on all the Bank's assets to secure the deposit (R. S. 3466; World War Veterans' Act).

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WESTERFIELD-BONTE COMPANY, INCORPORATED, LOUISVILLE, KY.

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Jurisdictional Authority. A writ of *certiorari* granted October 24, 1932 (R. 19; —— U. S. ——), pursuant to Act. February 13, 1925, C. 229 §1, 43 Stat. 937; Jud. Code, 237 (b); 28 U. S. C. A. §344.

Statute of United States involved, R. S. 3466; 31 U. S. C. A. §191 (*Cf. U. S.* v. *Oklahoma*, 261 U. S. 253, 259).

Date of Judgment, etc., May 10, 1932 (R. 12); rehearing denied June 21, 1932 (R. 18); petition for *certiorari* filed September 21, 1932; petition granted October 24, 1932 (R. 19).

Nature of the Case, rulings, etc. Petitioner as Guardian of a mentally incompetent World War Veteran deposited his ward's War Risk Insurance money and Disability Compensation in a Bank, which later closed its doors because insolvent, and was taken charge of by the State Banking Commissioner for liquidation. Petitioner claims a preferance both under (1) R. S. 3466 and (2) 43 Stat. 613, 38 U. S. C. A. §450, 454, as against all other depositors. The Court of Appeals of Kentucky *denied* the preference so claimed (R. 12-17).

Supreme Court of the United States

October Term, 1932. No. 388.

LETCHER SPICER, BY SAM SPICER, GUARDIAN AND COMMITTEE, - - - - - - - - - - *Petitioner,*

v.

J. BRYAN SMITH, SPECIAL DEPUTY BANKING COMMISSIONER AND LIQUIDATING AGENT OF HARGIS BANK AND TRUST COMPANY.

On Writ of Certiorari to the Court of Appeals of Kentucky.

BRIEF FOR PETITIONER.

The question involved here is whether (under R. S. §3466 and the "World War Veterans' Act, 1924," §§21, 22 (43 Stat. 607, 613; 38 U. S. C. A., §§450, 454) the Guardian,* of an incompetent World War Veteran, who deposited his ward's funds (derived from War Risk Insurance and Disability Compensation) in a State Bank, is entitled to a

*In Kentucky, the person having the official statutory care of the estate of a mental incompetent is called a "Committee" (Ky. Stat., §2149); but his powers and duties are defined to be "the same as those of the guardian of an infant" (§2153). For convenience, the Petitioner will be called "Guardian," although he is technically described in this record as both Guardian and Committee (R. 1, 12).

preference over all ordinary depositors and creditors of the Bank, when the Bank closed its doors because insolvent, and its affairs were taken over by the State Banking Commissioner for liquidation.

The lower State Court decided that the Guardian had a preferred claim, prior to all others, against the assets of the Bank in the hands of the Banking Commissioner (R. 10).

The Court of Appeals of Kentucky *reversed* that decision, and held that the United States parted with all possession and control of the money when it was paid over to the Guardian; and that, hence, the indebtedness of the Bank to the Guardian was a mere unsecured debt, wholly controlled by the laws of Kentucky with respect to preference and priority; and that, under the Kentucky laws, the Guardian was not entitled to any preferential lien for the deposit (R. 12-17).

The Guardian contends (1) that the money in question remains United States funds while in his hands and until it passes into the actual physical possession and control of the Veteran himself, and that until such time the United States is entitled to a preference under R. S. §3466; and, (2) that as the World War Veterans' Act exempts such funds, even in the hands of the Veteran himself, from the claims of his creditors, *a fortiori*, the ordinary general creditors of the Bank can not, in effect, subject such money to a *pro rata* payment of their own claims against the insolvent Bank.

The Banking Commissioner, on the other hand, contends that when the United States once paid the War Risk In-

surance money and the disability compensation to the Veteran's legally appointed Guardian, who deposited the funds in a State Bank, the ordinary relation of debtor and creditor arose between the Bank and the Guardian, that the rights and priorities between the Bank and the Guardian depositor must be determined by the laws of Kentucky under which the Bank operated and was liquidated; and that, therefore, no such preference as the Guardian claims, exists.

STATEMENT OF THE CASE.

Letcher Spicer is a World War Veteran, who completely and permanently lost his mind and is confined in the United States Veterans' Hospital at Chillicothe, Ohio (R. 1-2).

Spicer had $10,000 War Risk Insurance payable in case of "total permanent disability," in monthly installments of $57.50 (R. 4); and, in addition, was entitled to certain Disability Compensation for total permanent disability contracted in the line of duty (40 Stat., c. 105, §§300, 302, pp. 405, 406).

On September 29, 1919, the petitioner, Sam Spicer, was duly appointed Guardian for the incompetent (R. 2).

For ten years, from January 1, 1920, to February 5, 1930, the Guardian collected and deposited in a Bank at Jackson, Kentucky, all the moneys which, as such Guardian, he received from the United States as War Risk Insurance and Disability Compensation for his ward (R. 2-3). The Guardian had demanded payment of the deposit

before the Bank closed its doors, but the Bank refused to pay the deposit (R. 3).

On February 6, 1930, the Bank voluntarily closed its doors (R. 2), at which time it owed to depositors and other creditors $800,000, of which $200,000 was a secured debt owing to Cincinnati and Louisville banks.

There was not over $300,000 all told (including excess collateral on the bank loans) available to pay the remaining $600,000 unsecured depositors, so that the Bank could not possibly pay more than 50% and "probably *much less* than 50%" to the depositors (R. 6, 7). Thereupon, the Banking Commissioner took possession of the Bank, and after some difficulty sustained his right to liquidate the Bank (*Com.* v. *Hargis Bank & Trust Co.*, 233 Ky. 801). When the Bank closed its doors on February 5, 1930, the Guardian had on deposit there $6,070.80, of which about half was from War Risk Insurance and the other half from Disability Compensation (R. 2, 3, 8).

The Guardian filed this suit in the Breathitt Circuit Court against the Banking Commissioner, seeking to recover $6,070.80, with 5% interest to January 1, 1930, as a preferred claim against all the assets of the Bank in the hands of the Banking Commissioner, upon the ground that it was a debt due to the United States, entitled to a preference under R. S. 3466 and under the World War Veterans' Act (R. 1-3).

The Banking Commissioner defended upon the ground that the Guardian was a mere, ordinary depositor, "only entitled to share ratably with the other depositors and creditors of this bank" (R. 7).

The lower court decided that the Guardian was entitled to recover the deposit as a preferred claim against the assets in the hands of the Banking Commissioner (R. 10).

The Court of Appeals *reversed* the case, upon the ground that when the United States paid the money to the Guardian, such payment was a complete and final discharge of the Government's liability to the soldier; that the funds were no longer moneys of the United States, but were moneys of the veteran, held for his benefit by his Guardian; that neither the Guardian nor the Bank were "*indebted* to the United States" in the sense of R. S. §3466; and that, consequently, the Guardian was not entitled to any lien or preference in the distribution of the insolvent Bank's assets (R. 12-17).

This Court granted a writ of *certiorari* (R. 19), presumably because of the conflict on that subject, between the Kentucky and Connecticut decisions (*Shippee, Bank Commr.,* v. *Commercial Trust Co.,* 161 Atl. 775, not yet officially reported) on the one hand, and the contrary decisions in Nebraska (*State* v. *First State Bank,* 121 Neb. 521), Missouri (*Butler* v. *Cantley,* 47 S. W. (2d) 258, not yet reported officially), Minnesota (*Anderson* v. *Olivia State Bank,* 243 N. W. 398, not yet reported officially), Illinois (*Nelson, Auditor,* v. *Colegrove & Co.,* Ill. App. Court, August 18, 1932, No. 8616, not reported officially), and Ohio (*Ramisch* v. *Fulton,* 180 N. E. 735, not reported officially); *Cf.* also Iowa (*Manning* v. *Spry,* 121 Ia. 191), and Virginia (*United States Veterans Bureau* v. *Thomas,* 156 Va. 902).

We insist:

1. The deposit was a "debt due to the United States," entitled to priority under R. S. §3466.

2. War Risk Insurance and Disability Compensation when deposited in Bank by a veteran's statutory guardian, is a sacred trust fund of United States' money impressed with an equitable lien, and not only exempted from seizure by the veteran's creditors, but also entitled to priority of payment before other creditors of the Bank.

It will be helpful to make a short

Review of the United States' Right of Priority Under R. S. §3466.

1. At common law, by sovereign prerogative the Crown had a priority in the payment of public debts over private creditors (*Rex* v. *Wells,* 16 East 278; *U. S.* v. *State Bank of N. C.,* 6 Pet. 29, 35; *U. S.* v. *Canal Bank,* 25 Fed. Cas. 277, 278); but the United States has no such prerogative, as there is no common law of the United States (*Id.: Price* v. *U. S.,* 269 U. S. 492, 499, 500; *Spokane County* v. *U. S.,* 279 U. S. 80, 92).

2. To remedy that situation, at the first session of the first Congress, the Act of July 31, 1789, c. 5, §21 (1 Stat. 42) was adopted, giving the United States priority in payment of certain debts in cases of insolvency; which was successively broadened by four Acts (1790-1798) cited in the margin,* so as to cover every kind of indebtedness due to the Government in cases of insolvency, absconding debtors, voluntary assignments, and acts of bankruptcy; culminating in the Act of March 2, 1799, c. 22, §65, 1 Stat.

*Act of Aug. 4, 1790, c. 35, §45, 1 Stat. 169; Act of May 2, 1792, c. 27, §18, 1 Stat. 263; Act of March 3, 1797, c. 20, §5, 1 Stat. 515; Act of July 11, 1798, c. 71, §15, 1 Stat. 594.

676, which continued in force for 75 years, until its re-enactment (with trifling changes designed to broaden its application) on December 1, 1873, as §3466, Rev. Stats., which is still in force.

§3466 appears as the first section of Title XXXVI of the Revised Statutes, entitled "DEBTS DUE BY OR TO THE UNITED STATES" as follows (31 U. S. C. A., §191):

> "Whenever any person indebted to the United States *is insolvent,* or whenever the estate of any deceased debtor, in the hands of the executors or administrators, is insufficient to pay all the debts due from the deceased, *the debts due to the United States shall be first satisfied;* and the priority hereby established shall extend as well to cases in which a debtor, not having sufficient property to pay all his debts, makes a *voluntary assignment* thereof, or in which the estate and effects of an absconding, concealed, or absent debtor are attached by process of law, as to cases in which an *act of bankruptcy* is committed."

3. Although the earlier acts used the phrase "in which an act of legal bankruptcy shall have been committed," it is very important to note that there was no national bankruptcy act in existence for over 90 years out of our 144 years of national life;* that the Acts of 1792, 1797 and

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*The several Bankruptcy Acts were respectively in force as follows:

Act April 4, 1800 (2 Stat. 19; repealed Dec. 19, 1803, 2 Stat. 248)	3 yrs.
Act Aug. 19, 1841 (5 Stat. 440; repealed March 3, 1843, 5 Stat. 614)	2 yrs.
Act March 2, 1867 (14 Stat. 517; repealed September 1, 1878, 20 Stat. 99)	11 yrs.
Act July 1, 1898 (30 Stat. 544)	27 yrs.
Bankruptcy Acts in force	43 yrs.

1799 were all passed *before* the adoption of any national bankruptcy act whatever; that there was no national bankruptcy act in existence for 63 years out of the 75 years of life of the Act of 1799; and that R. S., §3466, was also in force for nearly 20 years when there was no national bankruptcy act.

Therefore, the term "act of bankruptcy" as used in R. S. §3466 and the various priority statutes, was not limited exclusively to those *technical* "acts of bankruptcy" as variously defined, from time to time, in the different national Bankruptcy Acts; but it must be given a broader meaning, embracing, (1) various situations which arose when there was no national Bankruptcy Act in force, but which Congress had in mind as constituting "acts of bankruptcy" in the broader and more general sense; and, of course, (2) any technical "act of bankruptcy" as defined in any of the various Bankruptcy Acts.

The *priority* statutes were in force for nearly 100 years when there was *no* Bankruptcy Act in existence and when there could not be any adjudication in bankruptcy. Therefore, it is not a condition precedent that there should be any actual bankruptcy proceedings pending, in order to give the United States a priority on account of the commission of some "act of bankruptcy."

In other words, there are circumstances when the United States is entitled to its priority of payment upon the commission of an "act of bankruptcy," even though there is no actual Bankruptcy proceeding brought, or even Bankruptcy Act in force.

The exact meaning of the phrase "act of bankruptcy" as used in the priority statute, has never been fully defined by this Court.*

The Supreme Court's Construction of R. S. §3466.

Bearing these general considerations in mind, it may be said that the Act has been authoritatively construed by this Court in the following particulars:

I. The debtor's insolvency must be such that *all* his property will not be sufficient to pay *all* his debts (*U. S.* v. *Oklahoma*, 261 U. S. 253, 260, and cases there cited); but even such insolvency, *taken alone*, will *not* give to the United States a priority of payment (*Id.*). The insolvency must be *manifested* in one of the three modes pointed out in the latter part of the statute, which defines or explains the *meaning* of the insolvency referred to in the earlier part of the statute (*Id.*).

II. The Bankruptcy Act of 1867 reaffirmed the Act of 1797 (now §3466); and both acts made the same provision

*By reason of the fact that (1) the language of §3466 was thus adopted and crystallized before there was any national bankruptcy act defining an "act of bankruptcy" and subsequent acts have adopted varying definitions thereof, and (2) §3466 has been equally in force whether there were or were not any national bankruptcy acts in existence, and regardless of what their particular terms were, some confusion has arisen, and different parts of §3466 have overlapped; as, for example, for over 100 years a "voluntary assignment" was not an "act of bankruptcy" even under the short-lived National Bankruptcy Acts of 1800, 1841 or 1867; and it first became an "act of bankruptcy" under the Act of 1898 when it was called "a general assignment for the benefit of his creditors."

with respect to the priority of payment of "all debts due to the United States" (14 Stat. 531; *Lewis Trustee* v. *U. S.*, 92 U. S. 618; *Guarantee Co.* v. *Title Guaranty Co.*, 224 U. S. 152, 158).

The Act of 1867 expressly defined as one of the "acts of bankruptcy":

> "That any person * * * who, being a banker * * * has fraudulently stopped or suspended and not resumed payment of his commercial paper, within a period of fourteen days, shall be deemed to have committed an act of bankruptcy" (14 Stat. 536, §39).*

III. The Bankruptcy Act of 1898 modified the provisions of R. S. §3466 with respect to the extent of the Government's priority of payment in bankruptcy cases where wages were given priority of payment over *ordinary* Government debts (*Guarantee Co.* v. *Title Guaranty Co.*, 224 U. S. 152, 158); but the Government's claims for taxes have priority even over wages (*Oliver* v. *U. S.*, 268 U. S. 1); and in bankruptcy cases the United States' priority is limited to taxes only (*Davis* v. *Pringle*, 268 U. S. 315; *Price* v. *U. S.*, 269 U. S. 492, 499, 500; *Spokane County* v. *U. S.*, 279 U. S. 80, 92).

IV. By the 1926 Amendment to the Bankruptcy Act of 1898, it was expressly provided† that—

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*It was "an act of bankruptcy" when the bank suspended payment, even *without fraud*, if it did not resume payment within fourteen days (16 Am. & Eng. Encyl. of Law, 2d Ed. 672, Note 1).

†Apparently adopted to avoid the result of *U. S.* v. *Oklahoma*, 261 U. S. 253 (see *Standard Acc. Ins. Co.* v. *E. T. Sheftall & Co.*, 53 Fed. (2d) 40, 41).

> "*Acts of bankruptcy* by a person shall consist of * * * *while insolvent,* a receiver or trustee has been appointed, or *put in charge of his property*" (44 Stat. Pt. 2, p. 662; 11 U. S. C. A., §21).

The law is pretty well settled as to the United States' right to priority in the distribution of assets in *actual bankruptcy cases,* but the law has *not* been fully settled by this Court in the settlement of insolvent estates *outside of* the bankrupt courts.

In the case at bar, the Bank [Hargis Bank & Trust Company] was hopelessly insolvent in the strict *bankruptcy* "sense."

Contentions of the Parties.

The opposing contentions may be thus summarized:

1. The Guardian claims that R. S. §3466 has come into play, because the Bank committed "an act of bankruptcy" (1) in the technical sense as defined by the Amendment of 1926; (2) in the secondary sense as once expressly defined in the Bankruptcy Act of 1867; and (3) in the general sense that any bank that permanently closes its doors and refuses to pay its depositors has committed "an act of bankruptcy" within the meaning of R. S. §3466.

2. The Guardian contends that the money paid to him by the United States on account of the veteran's War Risk Insurance and Disability Compensation, is still the money of the United States which he as Guardian is merely holding for its account until it shall have been applied to the actual benefit of the veteran; and, hence, upon its deposit

in the Bank, such Bank became "indebted to the United States" within R. S. §3466.

3. The Guardian contends that, independently of any construction that may be given to R. S. §3466, the true meaning of the World War Veterans' Act is that money paid by the United States thereunder, shall not, under any circumstances, be subject to the claims of the creditors of the veteran; and that *a fortiori*, such money cannot be applied to satisfy *pro tanto* the claims of creditors of the Bank; but that such money was impressed with an equitable lien in favor of the United States when it was deposited in the Bank; and that the Bank, and all its creditors, are affected with notice that such a deposit by an incompetent veteran's Guardian is impressed with such equitable lien in favor of the United States to secure, at all events, the payment of the money to the veteran, without the interference of creditors, tax claims, or any other hazard.

4. The Banking Commissioner contends that when the United States paid the War Risk Insurance and Disability Compensation to the Guardian and he deposited it in Bank, it was not a deposit of the United States' money; but that the United States had parted with all title, possession and control of the money by paying it to the Guardian, and the Government was thereby released and discharged of all liability to the veteran; and that the deposit was due to the estate of the veteran, and, as such, is controlled solely by the laws of Kentucky with respect to the preference or priority of deposits.

SUMMARY OF POINTS DISCUSSED.

1. War risk insurance and disability compensation paid by the United States to the guardian of an incompetent veteran, remain the money of the United States so long as it is in the guardian's hands or subject to his control, as the guardian is a mere instrumentality of the United States for the disbursement of such money for the veteran's benefit.

The guardian's deposit of such money in a bank is a deposit of United States money, so that the bank is "indebted to the United States" therefor. (*Infra* 14–28.)

2. The bank was insolvent in the bankruptcy sense; and when it closed its doors, refused to pay its depositors, and was taken over by the Banking Commissioner for liquidation, it committed "an act of bankruptcy" within the meaning of R. S. §3466, so that the United States is entitled to a preference in the repayment to it of the guardian's deposit in the bank. (*Infra* 29–31.)

3. Irrespective of R. S. §3466, the World War Veterans' Act does not permit any war risk insurance or disability compensation held by the guardian of an incompetent veteran to be subjected to the claims either of the veteran's creditors, or of the creditors of any bank in which the guardian has deposited such money. (*Infra* 32–36.)

FIRST POINT.

War risk insurance and disability compensation paid by the United States to the guardian of an incompetent veteran, remain the money of the United States so long as it is in the guardian's hands or subject to his control, as the guardian is a mere instrumentality of the United States for the disbursement of such money for the veteran's benefit.

The guardian's deposit of such money in a bank is a deposit of United States Money, so that the bank is "indebted to the United States" therefor.

Spicer had $10,000 War Risk Insurance and was totally and permanently disabled in the line of service (R. 2, 4).

By the War Risk Insurance Act of October 6, 1917 (40 Stat., c. 105, p. 398, *et seq.*), and the World War Veterans' Act, 1924 (43 Stat., c. 320, p. 607), it was provided that (1) if the veteran had taken the War Risk Insurance therein authorized, he should receive, in the case of total and permanent disability incurred in the line of duty, the amount of the insurance taken, payable in monthly installments; and (2) if he became totally and permanently disabled while in the line of service, he should receive certain sums as Disability Compensation.

Money paid, as here, by the United States, under the above Acts, on account of an incompetent veteran, is subject to the following special provisions:

The World War Veterans' Act, 1924 (43 Stat. 607, 613, 614; 38 U. S. C. A., §§421, 450, 451, 454), provides as follows:

"Sec. 21. That where any payment under this Act is to be made to * * * a person *mentally incompetent* * * * such payment may be made to the person who is constituted guardian * * * by the laws of the State or residence of claimant, or is otherwise legally vested with responsibility or care of the claimant or his estate * * *. *And provided further,* That the director, in his discretion, may suspend such payments to any such guardian * * * who shall neglect or refuse, after reasonable notice, to render an account to the director from time to time showing the application of such payments for the benefit of such minor or incompetent beneficiary.

"Sec. 22. That the compensation, insurance, and maintenance and support allowance payable under Titles II, III, and IV, respectively, *shall not be assignable;** *shall not be subject to the claims of creditors* of any person to whom an award is made under Titles II, III, or IV; and shall be *exempt from all taxation: Provided,* That such compensation, insurance, and maintenance and support allowance shall be *subject to any claims which the United States may have,* under Titles II, III, IV, and V against the person on whose account the compensation, insurance, or maintenance and support allowance is payable.

"Sec. 26. * * * That in cases where the estate of the decedent would escheat under the laws of the place of his residence, such instalments [*i. e.*, monthly instalments of compensation, yearly renewable term insurance, etc.] shall not be paid to the estate of the decedent, but *shall escheat to the United States* and

*By the War Risk Insurance Act of October 6, 1917, §402, under which Spicer originally received his War Risk Insurance policy, it was provided (40 Stat. 409):

"The insurance shall not be assignable, and shall not be subject to the claims of creditors of the insured or of the beneficiary."

shall be credited to the appropriation from which the original award was made."

Sec. 505 added by the Act of March 4, 1925 (43 Stat., c. 553, §20, p. 1312), makes embezzlement by a guardian a Federal offense, as follows:

> "Sec. 505. *Every guardian,* curator, conservator, committee or person legally vested with the responsibility or care of the claimant or his estate, having charge and custody in a fiduciary capacity of money paid, under the War Risk Insurance Act as amended, or under the World War Veterans Act, 1924, for the benefit of any minor or incompetent claimant, *who shall embezzle* the same in violation of his trust or fraudulently convert the same to his own use, *shall be punished* by fine not exceeding $2,000 or imprisonment at hard labor for a term not exceeding five years, or both." (38 U. S. C. A., §556.)

The Act of July 3, 1930, c. 849, §5, 46 Stat. 993; 38 U. S. C. A., §450, provides that in the event of the death of an incompetent veteran before receiving all of the War Risk Insurance or Disability Compensation to which he was entitled, or if, at his death, there are any such funds in the hands of his Guardian:

> "*Provided,* That payment will not be made to his personal representative if, under the law of the State of his last legal residence, his estate would escheat to the State; *provided further,* That any funds in the hands of a guardian, curator, conservator, or person legally vested with the care of the veteran or his estate, derived from compensation, automatic or term insurance payable under the War Risk Insurance Act as amended, or this chapter which, under the law of

> the State wherein the veteran had his last legal residence would escheat to the State, *shall escheat to the United States** and shall be returned by such guardian, curator, conservator, or person legally vested with the care of the veteran or his estate * * * to the bureau * * *."

The Act of July 3, 1930, c. 849, §21 (46 Stat. 1000; 38 U. S. C. A., §501a), provides:

> "That where an incompetent veteran receiving disability compensation under the provisions of this chapter disappears, the director, in his discretion, *may pay to the dependents* of such veteran the amount of compensation provided in §472 of this title for dependents of veterans."

By the foregoing statutory provisions, Congress clearly evidenced its intention that as to all moneys to be paid by it for the benefit of an incompetent veteran, such moneys should be

"*exempt* from all taxation,"
"should *not* be assignable,"
should "*not* be subject to the claims of creditors"; *but*
should *remain* "subject to any claims which the *United States* may have" against the veteran.

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*The Act of July 2, 1926, §3 (44 Stat. 792), provides with respect to unpaid instalments at the death of the veteran:

> "That in cases where the estate of the decedent would escheat under the laws of the place of his residence, such instalments shall not be paid to the estate of the decedent, but shall *escheat to the United States* and shall be credited to the appropriation from which the original award was made."

And further:

That the United States might *discontinue* payments to the incompetent veteran guardian if it thought proper. That, in the event of the veteran's death, if under the laws of the state of his residence the funds paid or unpaid would escheat to the State, such laws should not prevail, but such funds should escheat to the *United States.*

The real effect of all these provisions is that the money paid to the Guardian of an incompetent veteran, *remains the money of the United States* and largely subject to its control and to its direction regarding its ultimate disposition.

If such is the true relation of the United States to the money, then when Spicer's Guardian deposited the money in the Bank, it was a deposit of *United States money,* so that the Bank thereby became indebted to the United States therefor.

By the Constitution (Art. 1, §8, Cl. 1, 11-18), Congress is given the power to collect taxes in order to provide for the common defense and general welfare of the United States, to declare war, raise and support armies and navies, regulate the land and naval forces, govern the militia, etc.

Under those comprehensive powers, Congress can appropriate money for pensions, bounties, etc., and attach thereto such conditions regarding the disbursement, preservation, control and application thereof, as it may seem necessary and proper, including the right to fix by law the time and manner in which the pension or bounty shall finally pass to the recipient (*U. S.* v. *Hall,* 98 U. S. 343, 355;

Eckert & Co. v. *McKee,* 9 Bush (Ky.), 355; *Kellogg* v. *Waite and Trustee,* 12 Allen (Mass.), 529, 530. For an illuminating discussion of the powers of Congress in connection with the appropriation of public money, with many historical illustrations, see Brief of CHARLES E. HUGHES, in *Smith* v. *Kansas City Title & Trust Co.,* 255 U. S. 180; on original hearing, pp. 23-27; and on rehearing, pp. 38-48).

Similarly, under the power to regulate commerce with the Indian Tribes (Art. 1, §8, Cl. 3), Congress has attached and enforced a variety of conditions connected with the property and funds of the Indians, upon the general theory that the United States can constitute itself, and such agencies as it may adopt, guardian of the Indians' property and interests, in order to protect (1) the Indians from the loss or misappropriation of their money and property, and (2) the money paid by the United States for the benefit of the Indians, from any hazard of loss, dissipation or misappropriation until it shall have been actually used or enjoyed by the Indian himself for his own benefit.

The close analogy between pensions, War Risk Insurance and Disability Compensation, held by a guardian for the benefit of a mentally incompetent veteran, and Indian property held by the United States or one of its Indian Agents, for the benefit of the Indians, is so close that it will be sufficient to cite one or two pension and Indian cases to show that money paid by the United States to such guardian remains the money of the United States, until finally expended for the veteran's benefit; and that, consequently, while such money remains on deposit in a Bank, the bank is "indebted to the United States" for the amount of the deposit.

In *U. S.* v. *Hall*, 98 U. S. 343, Hall was the legal guardian under the laws of Ohio of an infant under 16 years of age. The infant was entitled to a certain pension. The United States paid the pension money to the local guardian who embezzled it. He was indicted under a Federal Statute. This Court held that Congress had the power to provide for the punishment of a State guardian who embezzled pension money which the United States paid to him for the use of his ward.

The ground of the decision was that, as Congress had the power to grant pensions and bounties, it also had the power to (p. 351)

> "pass laws to protect the fund appropriated for such a beneficiary of the Government, certainly until it reaches his hands. Congress in many cases has passed such laws and provided that the money shall not be transferable or subject to attachment, levy, or seizure, even after it has been received by the agent, attorney, or guardian."

After reviewing various statutes designed to protect pensioners from the loss or improvident use of pension money, it was held that, even after the money was paid to the guardian, it still remained within the constitutional control of the United States, with power in Congress to punish the guardian, if he embezzled it, for the following reasons (p. 357):

> "1. Because the United States, as the donors of the pensions, may, through the legislative department of the government, annex such conditions to the donation as they see fit, to insure its transmission unimpaired to the beneficiary. 2. Because the guardian no

more than the agent or attorney of the pensioner is obliged by the laws of Congress to receive the fund; but if he does, he must accept it subject to the annexed conditions. 3. Because the word 'guardian,' as used in the acts of Congress, *is merely the designation of the person* to whom the money granted may be paid for the use and benefit of the pensioners. 4. Because the fund proceeds from the United States, and inasmuch as the donation is a voluntary gift, the Congress may pass laws for its protection, certainly until it passes into the hands of the beneficiary, which is all that is necessary to decide in this case. 5. Because the elements of the offense defined by the act of Congress in question consist of the wrongful acts of the individual named in the indictment, wholly irrespective of the duties devolved upon him by the State law. 6. Because the theory of the defendant that the act of Congress augments, lessens, or makes any change in respect to the duties of a guardian under the State law is entirely erroneous, as the act of Congress merely provides that the pension may be paid to the person designated as guardian, for the use and benefit of the pensioner, and that the person who receives the pension, if he embezzles it or fraudulently converts it to his own use, shall be guilty of a misdemeanor, and be punished as therein provided."

In *Bramwell* v. *U. S. Fidelity Co.*, 269 U. S. 483 (S. C.), 295 Fed. 331 (D. C.), 299 Fed. 705 (C. C. A.), the Superintendent of an Indian Reservation deposited in Bank certain moneys received by him from the sale of tribal lands, Indian allotments, etc. It was held that the Bank was "indebted to the United States," because the United States is, in effect, the guardian of the Indians, and as such supervises and manages their affairs and collects and dis-

burses funds intended for their benefit. This Court said (269 U. S., at 487):

> "The lower courts rightly held that the amount owed by the bank on account of the deposit in question was a debt due to the United States."

The Circuit Court of Appeals, whose holding was thus approved, had said (299 Fed. 705):

> "Notwithstanding that the money on deposit with the bank stood in the name of the Indian agent and was held for the use and benefit of the Indians as their property, there can be no question but that it represented a debt due from the bank to the United States. This is recognized in the terms of the bond which was given to secure its payment, and it is the generally accepted doctrine as to all moneys held by officers of the United States in trust for the use and benefit of the Indians. The United States, under its treaty with the Klamath Indians, was the guardian of the Indians on the reservation. *United States* v. *Humason* (C. C.), 8 Fed. 71; *United States* v. *Fidelity Trust Co.*, 121 Fed. 766; *United States* v. *Comet Oil & Gas Co.* (C. C.), 187 Fed. 674; *United States* v. *Gray*, 201 Fed. 291; *Watson* v. *United States* (C. C. A.), 263 Fed. 700; *Central Nat. Bank of Tulsa* v. *United States* (C. C. A.), 283 Fed. 368; *United States* v. *State of Oklahoma*, 261 U. S. 253."

It was accordingly held in that case that, as the Bank was indebted to the United States, the latter had a prior lien on the Bank's assets under R. S., §3466.

The principle underlying both the *Hall* and *Bramwell* cases is that, where the United States has certain property or moneys which it desires to be applied for the benefit of

certain classes of people, whether pensioners or Indians, the *United States* is the real party in interest and can prescribe whatever terms it sees fit with respect to the title, control and disposition of its property and money, up to the time when the property and money has been actually received by the ultimate beneficiary. The consequence of this theory is that, in the meantime, *the property and money is the property and money of the United States,* the embezzlement of which it can punish, and for the security of which it can provide.

Therefore, when pension money is embezzled by a State guardian, it can be punished as the theft of United States money. When Indian money or pension money is deposited by the person charged with the duty of holding and applying it for the benefit of the beneficiary (whether such person is called "Indian agent" as to Indians, or "guardian" as to incompetent veterans), it is, in either case, *the money of the United States* which is being placed in the bank; the bank is "indebted to the United States" therefor, and the United States had the constitutional power to provide that it should have a prior lien upon the assets of the bank to secure the repayment to it of its money.

It should be borne in mind that there is no distinction between the position of the man appointed as Indian Agent by the United States, on the one hand, and the man, although appointed as guardian under the State law, who is selected by the United States as the agency or instrumentality for the holding and administration of the money of the United States to be applied for the benefit of the veteran. The guardian under a State law, who accepts

pension money, is just as much an agent or instrumentality of the United States with respect thereto, as is the person appointed by the United States as Indian Agent.

The fact that the guardian of an incompetent veteran holds his appointment under the probate court of a State, does not, in the slightest degree, lessen his allegiance or responsibility to the United States with respect to the money or property which the United States pays over to him for the use of his ward. In short, as a mere matter of administrative convenience, the United States selected the guardian under the probate court's appointment to carry out a Federal function, just as in 1917 the United States selected the election officers in the several States to carry out the provisions of the Draft Act. A person who, by virtue of having been an election officer under the State laws, was designated to carry out the Draft Act, was an instrumentality of the United States as fully and completely as if he had been initially so designated without ever having served as a State election officer.

In *U. S. Veterans' Bureau* v. *Thomas,* 156 Va. 902, it is said:

> "The Federal Government has adopted our State Courts as a means whereby the compensation of incompetent veterans of the World War may be administered and used for their benefit."

In accordance with the foregoing principles, the courts of numerous States have held, under a variety of circumstances, that when War Risk Insurance or Disability Compensation money was deposited in a bank by the veteran himself, or by a State guardian, or other fiduciary, the

bank was "indebted to the United States," which had a prior lien on the assets of the bank to secure the repayment of the deposit, for the benefit of the beneficiary.

REVIEW OF STATE COURT CASES.

In *State* v. *Security Bank*, 121 Neb. 515, a veteran died intestate, and his administratrix collected and deposited in the Security Bank the proceeds of the veteran's War Risk Insurance. The Bank failed. It was held that the money so paid by the United States as War Risk Insurance was not an asset of the estate; that the administratrix was a mere trustee to receive and pass on the funds to those entitled to them; and that

> "It is the money of the United States until it reaches the beneficiary, intended by the trust created. The Congress of the United States created a channel through which this money is to reach the dependents of the veteran. It must not be diverted from that channel. It cannot be so diverted. As money of the United States, it is entitled to priority by virtue of the Statutes of the United States."

It was held that under R. S., §3466, the Receiver of the failed bank was "indebted to the United States," which had a prior lien on the bank's assets for the amount of the deposit which the administratrix of the veteran had made therein.

In *State* v. *First State Bank*, 121 Neb. 521, a State Court appointed a guardian of a mentally incompetent World War veteran, who received from the Government both compensation and insurance, which he deposited in a State bank. The bank went into the hands of a receiver.

It was held that the moneys so deposited were funds of the United States, and that under R. S., §3466, the guardian had a lien prior to the other depositors of the bank. The Court said:

"The money is paid by the United States for the benefit of the disabled veteran or his beneficiary. The United States, for convenience, paid the money impressed with a trust provision to the guardian. Such guardian could not be required to accept money, but, if he accepted it, he took it subject to all the provisions imposed by statute. * * * We are of the opinion that the guardian in this case is the *instrumentality of the United States* for the purpose of paying the proceeds of War Risk Insurance to the beneficiary. *He is a mere trustee or depositary for the Government.* * * * Until the money is paid to the beneficiary, the obligation is not discharged. For convenience, in the case of an incompetent, the money is paid to the guardian. In such a case, the guardian is nothing more than an *agent of the Government* and the money in his hands is under its control and management. So long as the fund is subject to the control of the Federal Government, the State has no right to control it. Where War Risk Insurance is paid by the United States to the guardian of an incompetent, *the money belongs to the United States,* and is subject to its control until it reaches the beneficiary designated according to law. In such a case, the guardian is the agent for the Government and his authority over the fund is limited and controlled by Federal Statutes alone.

"Except as to $500, which it is stipulated was not proceeds of war risk insurance, the deposit represented funds of the United States, and as such is entitled to priority over claims of other deposits."

In *Butler* v. *Cantley*, 47 S. W. (2d) 258 (Mo.; not yet officially reported) a veteran died; his administrator collected over $5,000 from the United States Veterans' Bureau, as the proceeds of a War Risk Insurance Policy held by the veteran. The administrator deposited the money in a State bank, which subsequently closed, and was taken charge of by the State Commissioner of Finance. It was held that, under R. S., §3466, the administrator had a preferred claim, because it represented—

> "moneys belonging to the United States of America until it arrived in the hands of the intended beneficiaries of that fund, within the meaning of the statute disposing of that fund."

In *Anderson* v. *Olivia State Bank*, 243 N. W. 398 (Minn.; not yet officially reported) a World War Veteran was mentally incapacitated and totally and permanently disabled. A guardian was appointed for him, and deposited in a State Bank $1,354.08, partly from proceeds of War Risk Insurance and partly from proceeds of Disability Compensation. It was held that the guardian had a prior lien, both under the State and Federal statutes. The Court said:

> "Such funds do not vest in the ward until actually paid over to him, or until the funds are expended for his benefit. * * * The funds here involved belonged to the United States at the time the bank closed and remained such in the hands of the Commissioner of Banks."

In *Nelson, Auditor* v. *John B. Colegrove & Co.*, Ill. App. Ct. No. 8616 (decided August 18, 1932; not yet offi-

cially reported), a World War Veteran was permanently and totalled disabled. He had two minor children. Their mother was recognized [appointed] as their legal guardian by the Veterans' Bureau. She received from the Bureau various sums for the use of her wards as Compensation due them as minor children of a disabled veteran. She deposited the money in a State Bank, which became insolvent and went in the hands of a receiver.

Another veteran died, having a policy of War Risk Insurance. The State Court appointed a guardian for his minor brother, named as beneficiary for half of the insurance. The guardian received from time to time various sums of money, as the proceeds of the insurance, and deposited it in the State Bank which became insolvent.

It was held that, under R. S., §3466, the guardians had a preferred claim against the funds of the closed bank. The Court aptly said:

> "Payment of moneys to a guardian or conservator under this Act is not made to the guardian or conservator in his representative capacity as such, but as a representative of the Federal Government to whom he is required to account for his acts."

SECOND POINT.

The bank was insolvent in the bankruptcy sense.

When it closed its doors, refused to pay its depositors, and was taken over by the Banking Commissioner for liquidation, it committed "an act of bankruptcy" within the meaning of R. S. §3466, so that the United States is entitled under that statute to a preference in the repayment to it of the guardian's deposit in the bank.

R. S., §3466, reads as follows:

> "Whenever any person indebted to the United States is *insolvent*, or whenever the estate of any deceased debtor, in the hands of the executors or administrators, is insufficient to pay all the debts due from the deceased, the debts due to the United States shall be first satisfied; and the priority hereby established shall extend as well to cases in which a debtor, not having sufficient property to pay all his debts, makes a voluntary assignment thereof, or in which the estate and effects of an absconding, concealed, or absent debtor are attached by process of law, as to cases in which an *act of bankruptcy* is committed."

1. The Bank was "insolvent" within the meaning of R. S., §3466; *i. e.*, all its assets were not enough to pay all its debts (R. 6, 7) (*United States* v. *Oklahoma*, 261 U. S. 253, 260).

2. When the Bank refused to pay its depositors, closed its doors and was taken over by the Banking Commissioner for liquidation (R. 3, 6, 7), and has never since reopened, *ipso facto* that constituted "an act of bankruptcy" within the meaning of R. S., §3466, because:

(1) By the May 27, 1926, Amendment to the Bankruptcy Act (44 Stat. 662; 11 U. S. C. A., §21) "*acts of bankruptcy* by a person" are expressly defined to arise when

> "while insolvent, a receiver or a trustee has been appointed, or put in charge of his property."*

(2) The Bankruptcy Act of March 2, 1867, provided that a person should "be deemed to have committed an *act of bankruptcy*"

> "who, being a banker, merchant, or trader, has fraudulently stopped or suspended and not resumed payment of his commercial paper, within a period of fourteen days" (14 Stat. 517, 536, Section 39).†

(3) In the general sense (apart from technical statutory definitions), an *act of bankruptcy* is committed whenever a person refuses to pay his debts, closes his doors, and has his property taken over for liquidation by some public official.

We have shown under our First Point that the Bank was (*a*) "indebted to the United States"; and under this Second Point, we have shown that the Bank was both (*b*) insolvent and had (*c*) committed "an act of bankruptcy" within the meaning of R. S., §3466. Therefore, (*a*), (*b*)

**Cf. Standard Acc. Ins. Co.* v. *E. S. Sheftall & Co.*, 53 F. (2d) 40, 41.

†That statute has been construed to mean that the act of bankruptcy exists when the banker, even *without fraud*, suspends payment and does not resume payment within 14 days (16 Am. & Eng. Enc. of Law, 2d Ed., p. 672, note 1). Even though the Bankruptcy Act of 1867 was subsequently repealed, its definition of what constitutes "an act of bankruptcy" remains pertinent in determining what acts fall within R. S., §3466, because, as pointed out at p. 7, *supra*, §3466 has been in force during nearly 90 years when there was *no* Bankruptcy Act in force.

and (*c*) co-existing, it automatically results that the United States is entitled by the express terms of R. S., §3466, to a priority in payment of the Spicer deposit before the other depositors of the bank are paid.

United States v. *Oklahoma,* 261 U. S. 253, is inapplicable. In that case, the United States, as guardian of incompetent Indians, caused certain Indian moneys to be deposited in a bank which was later taken over by the State Banking Commissioner. This Court held that the United States was not entitled to priority under R. S., §3466, because: (1) the bank, while insolvent under the Oklahoma law so as to justify its seizure by the Banking Commissioner, was *not* insolvent in the *bankruptcy sense* required by R. S., §3466, *i. e.*, "not having sufficient property to pay all his debts," (2) there was no "act of bankruptcy" committed, because the bank took no action whatever to place itself in the hands of the Banking Commissioner nor did it make a voluntary assignment of its property, and (3) the case arose *before* the May 27, 1926, Amendment to the Bankruptcy Act which definitely prescribed (apparently in view of the decision in *United States* v. *Oklahoma*) that an act of bankruptcy should be deemed to exist where "while insolvent a receiver or a trustee has been appointed or put in charge of his property."

THIRD POINT.

Irrespective of R. S. §3466, the World War Veterans' Act does not permit any war risk insurance or disability compensation held by the guardian of an incompetent veteran to be subjected to the claims either of the veteran's creditors, or of the creditors of any bank in which the guardian has deposited such money.

By the World War Veterans' Act (p. 14 *et seq., supra*), Congress provided that any insurance, compensation, or other allowance which it made for an incompetent veteran (1) should not be assignable, should not be subject to claims of the veteran's creditors and should be exempt from taxation; but (2) should be subject only to any claim which the *United States* might have against the veteran; (3) that where the veteran's estate was about to escheat, any unpaid installments or money on hand should not go to the State, but should escheat to the *United States;* and (4) any guardian of an incompetent veteran who embezzled such insurance, compensation or allowance should be punished for a Federal offense.

Numerous state courts have construed the World War Veterans' Act to mean that Congress intended to hold control of the money until it reached the hands of the veteran himself; that under no circumstances should any creditor or other person be able to seize the money prior to the time that the veteran himself got it; that if prior to the time the veteran himself received it, the money should be held by any one, or deposited in a bank, it was in effect impressed with an equitable lien in favor of the United

States for the benefit of the veteran, of which every custodian or bank was affected with notice; and that consequently, where the guardian of an incompetent veteran or his minor children, deposited the proceeds of the veteran's war risk insurance, disability compensation, or other allowance in a bank which thereafter became insolvent and failed, such guardian could recover the deposit as a preferred claim ahead of all other depositors.

These decisions were not based upon the theory that the title to the money was still in the United States, so that the bank was indebted to the United States, and hence, R. S., §3466, gave a prior lien to the United States (see cases p. 25 *et seq., supra*), but they were based upon the broader and slightly different ground that when the United States paid the money to a guardian or other fiduciary, it was for the use and benefit of the veteran or his dependents, and was *impressed with an equitable lien* in favor of the veteran or his dependents to the end that all persons who came into possession or custody of the money, with knowledge of the source from which the money was derived, were affected with notice of such equitable lien. (See *U. S.* v. *Butterworth Judson Corp.*, 267 U. S. 387, 393, and cases cited.)

Therefore, when any bank received from the guardian of a veteran a deposit of War Risk Insurance or disability compensation money, the bank held it as a special trust fund impressed with an equitable lien in favor of the guardian; and in the event of the bank's insolvency, the guardian was entitled to recover the money in priority to other depositors.

Or, stated a little differently, the Government paid the money to the veterans' guardian with the condition attached that the money could not in any event be subjected to the taxing power of the State, to any levy by the veteran's creditors, nor be voluntarily assigned by the veteran himself or escheated to the State. In short, Congress provided that no circumstance should deprive the veteran of receiving the full benefit of the Congressional payment or bounty.

If such were the intent of Congress, *a fortiori,* Congress never intended that the deposit of such money in a bank should, in the event of the bank's insolvency, be used to pay, in whole or in part, other depositors or creditors of the bank.

In *Ramisch* v. *Fulton,* 180 N. E. 735 (Ohio; not yet officially reported) Ramisch deposited in an Ohio savings bank a check which he had received from the Veterans' Bureau as a loan on an adjusted service certificate. Some five weeks later, the bank failed and was taken over by the Superintendent of Banks. Although it is settled law in Ohio that the relation of a bank to a depositor is that of debtor and creditor, and not of bailee or trustee, the Court held that the bank was bound to know that the proceeds of such a bonus loan were exempt from seizure, and that Ramisch was entitled to recover the full amount of the deposit.

In *In re Fisher's Estate,* 302 Pa. 516, it was said with reference to the proceeds of War Risk Insurance:

> "The fund arising from war risk insurance is an earmarked fund that has impressed on it the quality given to it by the United States government, the qual-

> ity of a national donation, bounty, or gift for services in defense of the nation. The fund may be traced through the various agencies until it reaches its final destination in consummation of the original purpose for its creation. The badge of national obligation to a soldier protects it from liability for taxes, debts, and the like; * * * The fund is not part of the deceased soldier's estate as such, but is an earmarked fund, having certain special characteristics,"

In *Tama County* v. *Kepler*, 187 Iowa 34, a pensioner became insane, and the United States paid the pension money to his legal guardian. After his death, it was held that the County could not recover from the administrator the expense of the pensioner's maintenance at the County Poor House. The Court said:

> "In this case it appears that the insane person was under guardianship, and that the moneys or funds which the plaintiff seeks to subject to the payment of its claim were never delivered to the pensioner, but were paid over to his guardian, and, so far as appears, remained in his hands to the end of the pensioner's life. It is the settled law of the United States and of this State that the guardian in such case 'is nothing more than an agent for the Government, and that (pension) money in his hands is still under its control and management.'"

In *Payne* v. *Jordan*, 36 Ga. App. 787, the beneficiary of a War Risk Insurance policy received her monthly check and invested the proceeds in a house and lot. It was held that the house and lot thus purchased were not subject to execution. This carries the doctrine of equitable lien to the extreme limit.

In an earlier case of *Payne* v. *Jordan,* 152 Ga. 367, it was held that even after the proceeds of a War Risk Insurance policy were paid to the beneficiary who had deposited the same in a bank, they were not subject to garnishment.

In *In re Murphy's Committee,* 134 Misc. 683, it was held with respect to an incompetent veteran:

> "It seems unjust that the law should prevent the committee of an incompetent veteran from paying a person or agency, who or which, without the proper authorization of the committee, has furnished necessary support and maintenance to such veteran, but persons and agencies dealing with incompetent veterans are chargeable with the knowledge that the law jealously protects their allowances against their claims, and they must suffer the consequences."

CONCLUSION.

Whether this case be considered from the standpoint of the money being that of the United States, to whom the Bank was indebted, and hence the United States has priority under R. S., §3466, or from the standpoint (regardless of R. S., §3466), that the various statutes governing World War Veterans' payments evidence an intention that no one can acquire any title to the money, except the veteran himself, and that the money is impressed with an equitable lien to that end—in either event, the result is the same. The Bank must, to the extent of its assets, pay the deposit back to the Guardian of Letcher Spicer.

The opinion and judgment of the Court of Appeals of Kentucky should be reversed, and the decision of the Breathitt Circuit Court should be approved.

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January 17, 1933.